Supreme Court, U.S.
FILED
FEB 6 1987
JOSEPH F. SPANIOL, JR.
CLERK

No. 86-611

In the Supreme Court of the United States

OCTOBER TERM, 1986

COSMO J. CATERINO, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

CHARLES FRIED
Solicitor General

ROGER M. OLSEN
Assistant Attorney General

WYNETTE J. HEWETT
MURRAY S. HORWITZ
Attorneys

Department of Justice
Washington, D.C. 20530
(202) 633-2217

13 pp

QUESTIONS PRESENTED

1. Whether the court of appeals misapplied the "willfulness" requirement of Section 6672 of the Internal Revenue Code.

2. Whether the court of appeals erred in affirming the judgment of Section 6672 liability despite the district court's failure to make an explicit finding that petitioner had acted "willfully."

BEST AVA

TABLE OF CONTENTS

	Page
Opinions below	1
Jurisdiction	1
Statement	2
Argument	6
Conclusion	10

TABLE OF AUTHORITIES

Cases:

Gulf Towing Co. v. *Steam Tanker, Amoco New York*, 648 F.2d 242 (5th Cir. 1981) 9

Harrington v. *United States*, 504 F.2d 1306 (1st Cir. 1974) 7

Liddon v. *United States*, 448 F.2d 509 (5th Cir. 1971), cert. denied, 406 U.S. 918 (1972) 7

Slodov v. *United States*, 436 U.S. 238 (1978) 8, 9

Snider v. *United States*, 655 F.2d 729 (6th Cir. 1981) 7

United States v. *Pomponio*, 635 F.2d 293 (4th Cir. 1980) 7

Statute and rule:

Internal Revenue Code (26 U.S.C.):

§ 6672 ..... 2, 3, 4, 5, 7, 8

§ 6672(a) 3, 6, 7

Fed. R. Civ. P. 52(a) 9, 10

ILABLE COPY

In the Supreme Court of the United States

OCTOBER TERM, 1986

No. 86-611

COSMO J. CATERINO, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals entered on June 4, 1986 (Pet. App. 6a-16a), as amended on July 15, 1986 (Pet. App. 17a-21a), is reported at 794 F.2d 1. The opinion of the district court (Pet. App. 3a-5a) is unreported.

JURISDICTION

The judgment of the court of appeals was entered on June 4, 1986. A petition for rehearing was denied on July 15, 1986 (Pet. App. 17a). The petition for a writ of certiorari was filed on October 11, 1986. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. This case concerns petitioner's liability, under Section 6672 of the Internal Revenue Code,[1] as a "responsible person" of Northerlin Company during the first six months of 1974. Northerlin Company was a New York corporation that was experiencing financial problems. During 1973 and 1974, petitioner undertook a series of measures to assist Northerlin in surmounting these difficulties. In taking these steps, petitioner sometimes acted in his individual capacity, and at other times acted on behalf of Graham Stuart Corporation, a holding company of which petitioner was the president and controlling shareholder. Pet. App. 7a, 9a.

In early 1973, acting on behalf of Graham Stuart Corporation, petitioner commenced negotiations for the purchase of Northerlin's assets. These negotiations resulted in a written purchase agreement; the purchase was to have been consummated in August 1973, but it was postponed and never consummated. Pet. App. 9a. At various times during 1973, both before and after the scheduled purchase of assets, petitioner lent money, directly or indirectly, to Northerlin. He personally guaranteed a $240,000 bank loan to Northerlin in January 1973; he assisted Northerlin in obtaining a $500,000 bank loan in August 1973; and, acting as president of Graham Stuart Corporation, he lent $300,000 to Northerlin in October 1973 (*ibid.*). In January 1974, petitioner was instrumental in securing the replacement of Northerlin's general manager (*id.* at 10a). This change in management followed an agreement between petitioner and Northerlin's then-majority stockholder. Later that month, petitioner authorized certain Northerlin employees to transfer funds by telephone from a bank account established by Graham Stuart Corporation for Northerlin's use (*id.* at 9a-10a).

---

[1]Unless otherwise noted, all statutory references are to the Internal Revenue Code (26 U.S.C.), as amended (the Code or I.R.C.).

Early in 1974, the prospects for keeping Northerlin afloat worsened, and Northerlin's officers abandoned the company (Pet. App. 10a). Subsequently, a Northerlin employee prepared Northerlin's first quarter 1974 payroll tax return—that is, IRS Form 941, which reports, inter alia, federal taxes withheld from the wages of employees—and mailed it to petitioner. Petitioner sought the advice of Graham Stuart's accountant, who advised that Graham Stuart's bookkeeper should sign Northerlin's return as "agent" and mail it to the IRS. Petitioner then instructed the bookkeeper to sign the form as agent and mail it, and the bookkeeper did so (C.A. App. 71-72, 201-202, 209, 212-213). No payment of taxes accompanied this return. Similarly, in July 1974, Graham Stuart received Northerlin's completed but unsigned Form 941 for the second quarter of 1974. The bookkeeper, at petitioner's direction, signed the return and sent it in; once again, no payment of taxes accompanied the return. Prior to the filing of Northerlin's second quarter return—that is, on June 3, 1974—petitioner purchased all of Northerlin's outstanding stock and became the sole owner of the company. Pet. App. 10a.

2. Section 6672(a) of the Internal Revenue Code provides that "[a]ny person required to collect, truthfully account for, and pay over any tax * * * who willfully fails to collect such tax or truthfully account for and pay over such tax, * * * shall * * * be liable to a penalty equal to the total amount of the tax * * * not collected, or not accounted for and paid over." In April 1977, the IRS determined that petitioner was a "responsible person" of Northerlin, within the meaning of Section 6672, during all of 1973 and during the first two quarters of 1974. The Commissioner accordingly made an assessment of a penalty against petitioner in the amount of $510,010.41, representing the amount of Northerlin's unpaid withholding taxes for those periods. Petitioner paid the withholding taxes for

one employee for the first quarter of 1973 and filed a claim for refund with the IRS, which was denied. Petitioner then instituted a refund suit in the United States District Court for the District of Massachusetts, and the government counterclaimed for the balance of the assessment. Pet. App. 10a-11a.

Following a two-day trial, the district court issued an oral opinion, in which it held that petitioner was not a person responsible for the payment of Northerlin's withholding taxes, and hence was not subject to Section 6672 liability, at any time during 1973. The court held, however, that petitioner was a "responsible person" of Northerlin, and hence was subject to Section 6672 liability, during the first two quarters of 1974 (Pet. App. 1a-2a). The court accordingly entered judgment against petitioner requiring him to pay a penalty in the amount of Northerlin's unpaid withholding taxes for that six-month period. On petitioner's appeal, the court of appeals issued an unpublished opinion, stating that it was "unable to discern the critical findings and theory upon which the district court awarded judgment to the United States for the first two quarters of 1974." Accordingly, it vacated the judgment and remanded for clarification. See *id.* at 11a.

On remand, the district court entered a memorandum and order reaffirming its previous holding that the United States was entitled to prevail on its counterclaim for the first two quarters of 1974 (Pet. App. 3a-5a). The court explained that the filing of payroll tax returns on behalf of Northerlin by petitioner's accountant, while not dispositive of petitioner's status as a responsible person of Northerlin, was "at least some evidence of the devolution of control to [petitioner] by default, and his assumption thereof" (*id.* at 5a). The court also found "not credible" petitioner's testimony that he asserted no control over the daily affairs of Northerlin during the first half of 1974 (*id.* at 4a). The court based this credibility determination on the facts that no one else

was "in titular charge of Northerlin's business" during this period; that petitioner had made a "very large investment of his personal funds" in Northerlin; and that petitioner had "regularly monitored the operations of [Northerlin's previous managers] while they were nominally in charge of the business" (*id.* at 4a-5a). The district court accordingly concluded that petitioner had not carried his burden of proving that he was not a "responsible person" of Northerlin for the first two quarters of 1974 (*id.* at 5a). The district court's opinion focused on the responsibility question and did not contain a finding of fact specifically directed to whether petitioner had "willfully" failed to pay the taxes.

3. The court of appeals unanimously affirmed (Pet. App. 6a-16a, 19a-21a), concluding that the district court's finding of Section 6672 liability for the first two quarters of 1974 was not clearly erroneous. Specifically, the court of appeals upheld the district court's findings that petitioner had significant control over Northerlin and that he had, by early April 1974, sufficient power to decide which of Northerlin's creditors would be paid (*id.* at 12a-15a). With respect to willfulness, the court defined that term as "the voluntary, conscious and intentional decision to prefer other creditors to the United States" (*id.* at 15a (quotation marks and citations omitted)). The court explained that "[e]vil motive and specific intent are not necessary elements," and that a responsible person acts willfully if he "knows the taxes are not paid and allows the business to pay other creditors" (*ibid.*). The court of appeals pointed out that petitioner indisputably knew of Northerlin's unpaid 1973 taxes in early 1974, and that he indisputably learned of Northerlin's unpaid 1974 taxes when he received its quarterly payroll tax returns in April and July of that year. The court therefore concluded that the "willfulness" test was satisfied (*ibid.*).

In response to petitioner's petition for rehearing, the court of appeals added the fact that the district court had made no explicit finding of willfulness (Pet. App. 19a-21a). The court stated that such a finding "would have facilitated [its] evaluation as to whether willfulness was present," but concluded that such a finding was not indispensable where, as here, "a complete understanding of the issue[ ] is possible in the absence of separate findings" and the record clearly demonstrates the presence of willfulness (*id.* at 21a n.2 (quotation marks and citations omitted)). Accordingly, it concluded that the district court's failure to make a specific finding regarding willfulness was not reversible error.

ARGUMENT

Section 6672(a) of the Code imposes a penalty for failure to pay withholding taxes upon "[a]ny person required to collect, truthfully account for, and pay over" those taxes who "willfully fails" to do so. Thus, there are two elements to the imposition of such liability—the person must be a "responsible person" (that is, a person "required to collect * * * and pay over" the taxes) and his failure must be "willful." In the trial court, petitioner focused his efforts on attempting to show that he was not "responsible" for Northerlin's failure to pay withholding taxes (see Pet. 3-4; C.A. App. 11, 14, 254-261). The district court agreed with his contention with respect to Northerlin's 1973 taxes but disagreed with respect to Northerlin's delinquent taxes for the first two quarters of 1974 (see Pet. App. 12a-15a). Petitioner does not now challenge that aspect of the district court's decision, which was affirmed by the court of appeals. Instead, petitioner challenges the holding that his failure to pay the taxes for the first two quarters of 1974 was "willful." His contentions in this regard, however, were correctly rejected by the court of appeals, and there is no conflict in the circuits on the issues raised here. Accordingly, there is no basis for review by this Court.

1. Petitioner first contends (Pet. 8-10) that the court of appeals applied an incorrect legal standard in concluding that he acted "willfully," and that the standard applied by the court below is at odds with that applied in other circuits. This contention is without merit. The court of appeals defined "willfulness" for purposes of Section 6672(a) as a " 'voluntary, conscious, and intentional decision to prefer other creditors to the United States' " (Pet. App. 15a, quoting *Harrington* v. *United States*, 504 F.2d 1306, 1311 (1st Cir. 1974)). This definition is indistinguishable from the definitions quoted by petitioner (see Pet. 8-9) from decisions of other circuits that are said to conflict with the decision below. Indeed, most of the cases relied upon by petitioner were cited approvingly by the court of appeals in this case (compare Pet. 8-9 with Pet. App. 15a). Accordingly, petitioner's suggestion that the decision below announces a new "willfulness" standard that is inconsistent with that applied in other circuits is without foundation.

Petitioner's contention in this regard appears to boil down to the assertion that the courts below erred in finding willfulness on the facts here, "where there was no proof of either a diversion of funds or preference of other creditors, nor any proof that there were funds available" (Pet. 8). This contention fails for two reasons. First, petitioner can secure no advantage from any supposed failure of proof. When withholding taxes are not paid, the person against whom a Section 6672 assessment has been made bears the burden of proving either that he was not responsible for the default or that his failure was not willful. See, *e.g.*, *Snider* v. *United States*, 655 F.2d 729, 731 (6th Cir. 1981); *United States* v. *Pomponio*, 635 F.2d 293, 296 (4th Cir. 1980); *Liddon* v. *United States*, 448 F.2d 509, 513-514 (5th Cir. 1971), cert. denied, 406 U.S. 918 (1972). If petitioner had a valid claim that he did not act "willfully" in failing to pay the government, on the theory that Northerlin had no funds with

which to pay *any* creditor, it was his burden to prove that lack of funds. It was not the government's burden to prove that Northerlin had such funds available. Accordingly, the court of appeals correctly rejected this argument on the ground that petitioner had the "burden of proof in this proceeding and he never attempted to meet it on this issue" (Pet. App. 21a).

In any event, petitioner's premise—that Northerlin had no funds with which it conceivably could have paid its withholding taxes for the first two quarters of 1974—is belied by the record, which clearly shows that petitioner's conduct was willful. Petitioner himself admitted at trial that he knew Northerlin's taxes were not being paid (C.A. App. 69-70, 133-134). And he directed his employee to sign Northerlin's payroll tax returns and send them to the IRS without directing that the taxes be paid (see Pet. App. 15a, 20a). The availability of funds on Northerlin's part is established by the fact that, in January 1974, petitioner wrote to an Ohio bank authorizing Northerlin's employees to draw funds from one of Graham Stuart's accounts (*id.* at 10a). The availability of funds is further established by the fact that Northerlin continued to pay its employees' wages throughout the first six months of 1984. Thus, the record supports the conclusion that, during the period that petitioner was responsible for the payment of Northerlin's withholding taxes and with his knowledge, the company continued its operations by paying other creditors in preference to the United States. Accordingly, the record justifies the imposition of Section 6672 liability upon petitioner for the first two quarters of 1974.

Petitioner's reliance (Pet. 7, 9-11) on *Slodov* v. *United States*, 436 U.S. 238 (1978), is misplaced. In that case, the officer against whom the Section 6672 penalty was asserted had assumed control of the corporation "at a time when a delinquency existed for unpaid trust-fund taxes, while the

specific funds withheld but not paid had been dissipated by predecessor officers and when the corporation[ ] had no liquid assets with which to pay the overdue taxes" (*id.* at 246). The instant case is different in two critical respects. First, the tax delinquency in this case was not "inherited" by petitioner, as in *Slodov*; rather, the delinquency accrued during the six-month period in which petitioner was himself responsible for seeing that Northerlin's taxes were paid. Second, Northerlin did have funds with which it was continuing to operate, and petitioner deliberately chose not to use those funds to pay the United States. Petitioner's invocation of *Slodov* appears to rest on his assertion that he could not possibly have paid over the withholding taxes because of Northerlin's lack of funds—an assertion that must be rejected for the reasons stated above.

2. Petitioner also contends (Pet. 10-14) that the court of appeals erred in affirming the district court's judgment in the absence of a specific lower court finding of "willfulness." This contention is without merit for the reasons well stated by the court of appeals (Pet. App. 21a n.2). Petitioner acknowledges (Pet. 12) that the failure to make a finding of fact required by Fed. R. Civ. P. 52(a) does not require a remand "if a complete understanding of the issues is possible in the absence of separate findings and if there is a sufficient basis for the appellate court's consideration of the merits of the case" (*Gulf Towing Co.* v. *Steam Tanker, Amoco New York*, 648 F.2d 242, 245 (5th Cir. 1981)).

The court of appeals was clearly correct in finding that these conditions were satisfied here. The district court had specifically found "not credible" petitioner's testimony that, during early 1974, "he asserted no control over the daily affairs of Nortnerlin" (Pet. App. 4a-5a). The court further found that the filing of Northerlin's payroll tax returns "at [petitioner's] direction" was "some evidence of the devolution of control to [petitioner] by default, and his assumption thereof" (*id.* at 5a). The inferences from these findings

are clear. Petitioner knew that Northerlin's taxes were due and were not being paid. And he saw to it that funds were infused into Northerlin in order, as he testified, to "try[ ] to keep the company operating" (C.A. App. 78). Petitioner thus understood that Northerlin was paying its operating expenses without paying over to the government the requisite withholding taxes. Accordingly, the facts clearly justified a finding of willfulness, and no useful purpose would have been served by the court of appeals' remanding the case in order to have the district court enter an explicit finding on that point.[2]

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

CHARLES FRIED
Solicitor General

ROGER M. OLSEN
Assistant Attorney General

WYNETTE J. HEWETT
MURRAY S. HORWITZ
Attorneys

FEBRUARY 1987

---

[2]In light of the fact that this case was remanded once before to the district court for the entry of specific findings (see Pet. App. 11a), it cannot be suggested that the First Circuit is unaware of the importance of Rule 52(a) or that it is unwilling to enforce it by a remand in appropriate circumstances.